

*Please note: There have been changes in the sales tax rate procedures that affect the sales tax revenues coming to cities because of annexations and incorporations. Judy Cox, Public Finance Consultant, at the Municipal Research Services Center, provided the following information. For more information see Budget Suggestions 2001 on the Municipal Research Services Center web page at [www.mrsc.org](http://www.mrsc.org)*

## **Timing of Sales Tax Rate Changes (Ch. 104, Laws of 2000)**

In order to reduce the burden on retailers of dealing with sales tax rate changes, Ch. Chapter 104, Laws of 2000, ~~limits the effective date of sales tax rate changes to~~ requires that sales tax rate changes may take effect only on January 1, April 1, July 1, and or October 1. Limiting the number of dates on which rate changes can be made also makes a step in the direction of meeting the objections of those who say that Internet sales should not be taxed because there are too many different sales tax laws. Additionally, this law provides that local governments must notify the Department of Revenue (DOR) at least **75 days** before the change takes place.

### **So, what are the implications of this law for cities and counties?**

A city or county that wishes to increase its ~~optional sales tax~~ sales tax rate must make the change effective on one of those dates. This same ~~rule~~ requirement also applies to counties that want to levy the 0.1 percent criminal justice sales tax under RCW 82.14.340, the 0.1 percent tax for jails and juvenile detention facilities under RCW 82.14.350), the rural counties sales tax under RCW 82.14.370 and/or the rental car tax authorized in RCW 82.14.049. Public facilities districts taxing under RCW 82.14.390 and local transit taxes levied under RCW 82.14.045 also must follow these new requirements. Every sales tax levied under ch. 82.14 RCW is subject to the new law. Previously, a tax rate could be changed effective the first day of any month and there was no mandatory 75-day notice period.

This law applies not only to changes in a rate in an existing jurisdiction, it also applies to changes in geographic boundaries.

#### **?? *Effects on Incorporations***

~~Newly incorporated cities, all of whom, in recent years, have incorporated on the last day of February or August and levied the sales tax to be effective on the first day of March or September, will have to wait a month and levy the tax effective April 1 or October 1. In recent years, all new cities have incorporated on the last day of February or August and have levied the sales tax to be effective the next day (March 1 or September 1). This will not be possible under the new law. Cities that wish to incorporate in February or August may still do so but will have to wait a month and levy the sales tax effective April 1 or October 1. This scenario assumes that cities intending to incorporate provide DOR with the 75 days of advance notice required under the new law.~~

Because they will be levying the tax a month later than in the past, they will receive one month's less revenue than under past practice.

### ?? ***Effects on Annexations***

Cities may also want to take these dates into account when planning annexations. In order to maximize its sales tax revenue from the newly annexed area, the effective date of an annexation should now be the first day of a quarter – January 1, April 1, July 1, or October 1. Here are some examples of how things worked in the past and will change under this new law.

1. Effective date of annexation, January 1. Before the passage of this new law, DOR changed the tax code for the businesses in the annexed area on January 1, the retailers remitted the tax to DOR in February, and the city received its distribution at the end of March. Under the new law, exactly the same events will occur. The new law has had no effect on when the city gets its first sales tax from the annexed area. The lag in the receipt of sales tax revenues is simply a function of the time it takes to collect and distribute the money.

2. Effective date of annexation, February 1. In the past, DOR changed the tax codes on February 1 and, after receiving the tax receipts from the merchants in March, distributed to the city at the end of April. Now, a city that annexes effective February 1 will not be able to levy its sales tax in that area until April 1 (the first day of the next quarter) and will not receive any distributions from the annexed area until the end of June. Therefore, under the new law, the city receives two months less revenue from the annexed area if it annexes on February 1.

3. Effective date of annexation, March 1. Before the new law took effect, a city that annexed on March 1 had the tax codes in the annexed areas changed effective March 1 and got a distribution at the end of May from taxes DOR received in April. Now, a city that annexes at the beginning of March will receive one month's less revenue than in the past. The tax codes will not be changed until April 1 (the first day of the next quarter) and revenue collected during that month will not be distributed by DOR until the end of June.

To summarize, in the past, the date of the annexation had no effect on when the city received its sales tax from the annexed area – the lag between the time the tax was first levied and when it was distributed to the city was always the same. Under the new law, if a city annexes effective the first day of the second month of any quarter, it will receive two months less revenue than it would have under the old law. If it annexes effective the first day of the third month in a quarter, it will receive one month's less revenue. Only if it annexes on the first day of a quarter will this new law have no effect on its revenues compared to the prior law.

Note also that the new requirement that DOR be notified 75 days before first day of the month in which the city wants taxes to be collected further complicates matters. To start collecting sales tax on January 1, for example, the city council must have passed an ordinance approving the annexation by October 18. It may make sense in many cases (but it is not required by the new law) to set the effective date of the annexation at January 1 (in the example given here), rather than some earlier date, so that the city does not incur the expenses of serving the annexed area until it starts collecting the sales tax at the earliest possible date under the law. Under prior practice, the notice period for submitting reports of annexations and sales tax rate changes to DOR was much shorter

A county, city or town should inform the Department of Revenue, Local Sales Tax Section, at the following address, about an annexation, so that the department can make certain that the city jurisdiction receives its proper amount in the local distribution of the sales and use tax:

Local Tax Supervisor  
Department of Revenue  
General Administration Building  
PO Box 47476  
Olympia, WA 98504-7476  
Telephone: (360) 902-7103

The information that a city should provide includes:

- ?? The effective date of the annexation;
- ?? A legal description of the area;
- ?? A map of the annexed area; and
- ?? A copy of the annexation ordinance.

The city is responsible for informing the businesses in the annexed area about their new tax code and new tax rate. The city should give the department as much information as possible on the names of businesses in the annexed area, their addresses, and their unified business identifier (UBI). This information will assist the department in checking its records to make certain that the businesses are reporting properly and that the city is getting the proper amount of taxes from the annexed area.